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BOOK REVIEW

Christopher L. Culp: Structured finance & insurance – the ART of managing capital and risk

John Wiley & Sons, 892 pages, 95 USD/approx. 120 CHF

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This book is a comprehensive, self-contained overview of the field of alternative risk transfer (ART) and structured finance. I recommend this book to any practitioner dealing with structured finance and insurance for non-financial firms.

The book is based on an MBA course the author teaches at the University of Chicago's Graduate School of Business. Thus, its addressed audience is not financial engineers, but its intention is to connect corporate finance with risk-management practice and structured finance. The entire book contains a large quantity of real-world examples, which amplify its usefulness for anyone interested in understanding the applicability of structured finance for alternative risk transfer.

Culp's book is structured in five parts of which the first four are written by the author. The last part consists of nine chapters contributed by expert practitioners in the field.

The first part covers *Integrated Risk and Capital Management* and summarizes the theoretical fundamentals for the later parts. In the beginning, fundamental concepts of corporate finance and an introduction to risk management are repeated. Financial risks and risk induced by peril are distinguished, and further considered and classified as core or non-core risks for companies. Subsequently, the principal possibilities to manage these risks are exposed. The next three chapters of the first part summarize further topics of corporate finance. They cover debt-financing of firms, the arising problem of adverse selection and capital budgeting. Finally, the introduction to risk management is deepened by

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discussing the implications of risk transfer for corporate finance and by setting forth concepts of risk finance.

Part two of the book shows five possibilities of *Traditional Risk Transfer*. In separate chapters the mechanics of insurance, reinsurance, credit insurance, derivatives and credit derivatives are exploited. The exposition of the way of risk transfer is not aimed at the valuation of the respective products, however, the author carefully illustrates and explains the design and the mode of operation of the contracts.

Structured Finance is now broadly and deeply discussed as part three of the book. First, the author expounds the different types of structured financial solutions and the general structuring process. In the next two chapters, different types of structured finance corporate securities such as hybrids, convertibles and structured notes as well as contingent capital are introduced. Afterwards, the next six chapters deal with securitization and the disposition of credit risk, with the first of these – the fourth in this part of the book – chapters being a profound introduction to the field and giving many illustrative examples. Subsequently, the ideas and concepts from the first and the fourth chapter of the *Structured Finance* part are used in action: Collateralized Debt Obligations of cash and of synthetic type, probably one of the fastest growing markets for structured securities of the last decades, are described in principle in two short chapters. The last three chapters of this part deal with Structured Synthetic Hybrids, the Securitization of Private Equity and Hedge Funds as well as with Project and Principal Finance. Summarizing, this part of the book a comprehensive well-motivated overview of the current state and developments in structured finance and puts them on a common basis.

The fourth part of the book is dedicated to *Structured Insurance and Alternative Risk Transfer* and starts with a compendium on insurance-linked notes, thus, hooking up with the last chapters of the previous part. Commonalities are shown and these securities are distinguished from those of the former part. After this, the well-established concepts of captives, that is self-insurance structures, and of finite risk (re)insurance contracts are exemplified and the respective mechanisms are revealed. More complex insurance structures for integrated risk transfer, specifically multiline and multitrigger contracts are introduced thereafter. Finally, the fourth part of the book terminates with an short overlook on contingent cover, which is an option to enter an insurance contract.

Last, part five of the book supplements the former parts with nine essays which cover *Case and Issue Studies* written by expert practitioners in the respective fields. The topics covered range from the role and importance of patenting in finance over critical analyses of specific derivatives, insurance contracts and structured finance securities to warranty insurance.